MEMORANDUM

TO: Enron Files

FROM: Reed M. Brodsky

DATE: December 22, 2001

RE: Third Interview of Richard Causey

On December 21, 2001, Chuck Davidow, Joe Brenner and Reed Brodsky of Wilmer, Cutler & Pickering ("WCP") and John Sullivan and Jim Johnson of Deloitte & Touche (an accounting firm retained by WCP), spoke with Richard Causey, Enron's Executive Vice-President and Chief Accounting Officer, at Enron's Houston headquarters to gather information from him in order to allow WCP to provide legal advice to the Special Committee of Enron's Board of Directors. Jacks C. Nickens of Clements, O'Neill, Pierce, Nickens & Wilson, L.L.P., and Michael Levy and Amy Carpenter-Holmes of Swidler Berlin Shereff Friedman were present and represented Causey.

This memorandum has been prepared by counsel in anticipation of possible litigation arising from a Securities and Exchange Commission ("SEC") investigation and any parallel or related proceedings. This memorandum incorporates the mental impressions, analyses and opinions of counsel. As such, this memorandum is intended solely to assist counsel in providing legal representation and advice to the Special Committee of Enron's Board of Directors, and is not intended to provide a substantially verbatim recital of Causey's statements. The interview was based on WCP's understanding of the facts and review of documents as of the date of the interview. Furthermore, Causey has not reviewed this memorandum. Therefore, this memorandum may contain inaccuracies and the following discussion of certain events may be incomplete or lack context.

Davidow explained that, during our third interview with Causey, we would focus on LJM-related transactions, that we would ask open-ended questions, and that we were interested in Causey's recollection based on what he knew at the time of the events as opposed to what he has learned recently. Davidow further explained that, as during our prior interviews with Causey, the conversation was privileged but it was Enron's privilege, not his, and Enron alone has the ability to waive the privilege. Davidow stated that we were communicating with the SEC and other Government organizations seeking information.

Chewco

Causey did not recall having any role in the Chewco transaction. He was aware of the transaction at the time. He was aware that Chewco was a special purpose entity ("SPE"), Chewco was going to buy out CalPERS' interest in JEDI, and the transaction would create an unconsolidated subsidiary. Other than that, he had no further recollection of the transaction. He did not know how the transaction came to his attention; at the time, it was not raised as a significant transaction from an accounting perspective. Causey did not recall any accounting issues relating to Chewco coming to his attention this year before Chewco was consolidated retroactively as part of the November 2001 restatement. Causey recalled seeing the Chewbacca "head" that commemorated the transaction for the first time approximately one year ago.

Causey knew about Chewco's buyout of CalPERS' interest at the time it occurred. Andrew Fastow started talking about a potential buyout during the year prior to when it happened. Fastow was in charge of finance matters, and Causey had no objection to the transaction if Fastow wanted to do it. Causey did not recollect assisting on any accounting issues related to the transaction. By that time, structured finance groups were dispersed across business units and reported to Rodney Faldyn. Someone on Faldyn's team would have had responsibility for any accounting issues.

Causey was not certain whether Chewco was the first time that Enron used a SPE to deconsolidate something. Causey knew about Enron's use of SPEs previously in leasing transactions. He had spent time on a 1992 leasing transaction that involved a SPE. Causey also had some knowledge of SPEs before joining Enron. As a result, Causey was familiar indirectly with the 3% requirement. Chewco was handled by the finance, accounting, and legal groups in Enron's North America organization, which Enron called ECT at the time. ECT's then-CEO, John Nichols, would know about Chewco and probably had worked on the transaction.

Causey did not recall Michael Kopper's role in the Chewco transaction, Chewco's capital structure, or any other facts at the time. He did not remember hearing about the transaction at a Board or Board committee meeting. He understood that Ben Glisan and Jeremy Blachman, whose name appears on documents relating to Chewco, worked on the accounting side of the transaction. Causey would have expected Blachman to understand the significance of the loan-related papers.

When Chewco was consolidated recently, Causey had Arthur Andersen review the transaction. However, Causey repeated that he did not recall being involved in any accounting review of the transaction at the time it was structured. The accounting department in the business unit that oversaw the transaction would have reviewed it. Enron is a decentralized organization. Each business unit has an accounting group, a legal group, and a finance group. Each accounting group reports to its respective business unit and to Causey indirectly. In general, Causey worked with Nichols discussing issues that either he or Nichols had raised.

Causey typically signed the 10-Q's and 10-K's. He did not determine specifically that all transactions met SPE requirements. He addressed issues when they came up. He did not have a formal sign-off procedure. However, Causey made two points clear to his staff: (1) he expected full cooperation and openness with Andersen – Causey described this approach "open kimono" – and Andersen could look at whatever they wanted no matter who, what, when, or where; and (2) any auditing adjustment would be viewed as a failure and was unacceptable. Different accounting people in each business unit had the freedom to contact Andersen, and Causey encouraged them to contact Andersen directly. Causey did not know of any specific incidents of someone in a business unit being told not to contact Andersen. From a cost perspective, it was better and the preferred approach to have an accounting person communicate with Andersen. If a non-accounting person had the impression that he or she could not contact Andersen, it would surprise him, because it happened with some degree of regularity. It would be unusual if Andersen had been told that it could review the Chewco transaction documents only if Tom Bauer was the only person to review them and Bauer could not take any copies of documents back to Andersen with him. Such conditions would not be in keeping with the spirit of the open relationship that Causey had instructed his people to have with Andersen.

Enron does not have any list of Andersen contacts. Andersen had approximately 100 to 200 auditors on the scene in Houston at all times, and they became known to Enron people. The only Andersen people that consulted outside Houston directly with Enron (other than consultations with the national office) were in Calgary talking to the Canadian ECT. Enron does not have any list of topics that Andersen consulted on. Some of Andersen's bills itemized the matters subject to consultation, but others did not.

Causey did not receive a written document from each business unit explaining transactions. From time to time, he would have formal communications and one-on-one discussions of any important transaction that he was interested in hearing about.

Chewco came to Causey's attention again in or about October 2001 when he read in a Wall Street Journal article on a Thursday or Friday that Kopper had been involved in the transaction. There had been some "noise" internally about a related-party transaction involving Kopper. After reading the article, the Board requested an update on the transaction, and Glisan was charged with giving the Board the update. Causey did not know who had charged Glisan with this task. Faldyn, Christina Mordaunt, and others briefed Glisan on the transaction. Faldyn heard some things at these meetings that concerned him, and Faldyn brought them to Causey's attention. Causey and Faldyn reviewed the structure and were surprised by what they learned. Causey did not recall the details of what Faldyn reported to him, but it was obvious that the structure did not meet SPE requirements. It appeared that the structure did not have adequate equity. At that point, Causey alerted Dave Duncan at Andersen and then Ken Lay and Jim Derrick that he was concerned by the deal's structure. Causey told Lay and Derrick that he would monitor the situation.

Causey and Faldyn decided to get more people involved in the analysis, and Glisan suggested bringing in Bill Brown. Subsequent meetings were attended by, among others, Jeff McMahon, Glisan, Brown, Faldyn, Causey, and perhaps Mordaunt or another attorney. The structure was analyzed and discussed. Causey was told by someone, possibly Brown, that the structure was used temporarily to buy out CalPERS' interest, but another, normal SPE was to have been put in its place before the quarter ended. Someone, possibly Glisan, put this second structure on a blackboard, and it looked better.

Causey recalled analyzing the second structure and hoping that it would answer pending questions about the transaction. Causey was in a conference room on the twentieth floor with members of the finance team, Julia Murray, and Carol St. Clair. Causey and the finance team reviewed the structure, and attorneys reviewed documents. They were analyzing whether the equity was in proper form given that Kopper was part of the equity. Causey was troubled because the equity was exactly 3% and they might miss the 3% requirement by a small amount. The collateral arrangement came to the forefront. Duncan, Bauer, and possibly Deb Cash from Andersen were in the same room reviewing documents. Bauer was in charge of Enron's North America activity for the past five years. Causey, his team, and Andersen reviewed the collateral arrangement and concluded that it created a problem. Someone tracked down the relevant wire transfers to confirm the monetary amounts involved. During these meetings, they concentrated on determining what the structure was as opposed to why such a complicated structure was put together in the first place. Of those reviewing the documents and analyzing the structure, Glisan and Brown were trying to recollect what had happened while everyone else was trying to learn the facts for the first time.

Causey reported what he had learned to Lay and McMahon. Causey may have also reported to Derrick. Based on Causey's report, Lay understood that the new development with respect to the Chewco transaction could have an impact on Enron's earnings and debt. Causey did not believe that, prior to this time, Lay was familiar with SPE requirements; Causey did not believe that he had had a conversation with Lay previously about SPEs. When Causey learned about the reserve accounts and collateral arrangement, Causey did not question Glisan. Glisan had indicated that he was not aware of the collateral arrangement. Shortly thereafter, the Special Committee started its investigation, and Greg Whalley and Jeff McMahon instructed people to let the Special Committee conduct its investigation and not rush to judgment. As a result, Causey did not question Glisan more about what he knew and when he knew it. For the same reason, Causey did not question Blachman. Under different circumstances, Causey would have questioned Glisan and Blachman. Although Enron concluded that it had to restate its financial statements, Causey did not have a conversation with Blachman before the restatement. Causey did not talk with Duncan or Bauer about Chewco and what had happened. Andersen acted surprised by the revelations. Causey did not have a relationship with anyone at Barclays, and thus he did not speak with anyone there about the collateral arrangement. Causey did not know why the problem occurred with Chewco. He speculated that it was either a mistake or something more.

While the Special Committee was investigating, Causey formed a team headed by Faldyn and Chris Sherman to learn as much as possible about other SPEs and any other pending, related issues prior to the 10-Q for the third quarter. Their review was limited, because all relevant records were not immediately available. Faldyn and Sherman reported to Causey that they had not found any additional problems.

JEDI's earnings had an impact on Enron's earnings. The GAAP basis for allocating non-Enron stock prices to Enron changed over time. At some point, an idea was raised in favor of a special allocation to Enron of any non-Enron stock earnings out of the JEDI partnership. Causey did not remember whether this idea was memorialized. The allocation method was discussed, developed, and used in consultation with Arthur Andersen. Causey did not recall whether anyone raised any concern. Causey was involved with JEDI in or around 1992 and 1993, but over time he stopped working on it. From the beginning, there was an issue of how to deal with profits from Enron's stock.

LJM Governance

Fastow said that he had two equity partners in LJM1. Andersen audited the capital that was being invested in the partnership to verify that there was outside equity. Andersen asked Causey about LJM1's equity partners, and Causey directed Andersen to Fastow. Cash was charged with the responsibility of looking at LJM2's equity partners. Causey did not look into LJM's capitalization, and he did not know whether others looked into it. He relied on Andersen to analyze LJM's capitalization. Causey had a general understanding at the time that Andersen had looked at LJM's capital structure and, since Andersen never went back to Causey with any problems, Causey assumed that Andersen was satisfied with what it found. Andersen did not prepare a detailed audit report in writing, and there is no documentation regarding Andersen's review of LJM. Causey did not discuss LJM's capital structure with Fastow. Causey speculated that LJM could have used borrowed money in making investments so long as the loans were backed by firm equity commitments.

Causey agreed with Fastow that it would not be appropriate if Enron had unfettered access to LJM's financial statements. Causey attributed Fastow's sensitivity about disclosure of LJM's financial statements to the fact that LJM was a third-party and an independent entity. Andersen requested access to information about LJM and Fastow told Causey that Fastow had given Andersen all the information that Andersen requested.

Duncan shared his thoughts about procedures relating to LJM transactions with Causey, and they were adopted. Duncan's views related to Fastow's ability to control LJM and the ability of other LJM partners to remove Fastow. Causey saw the LJM1 partnership agreement, either in draft or final form, at some point, and he recalled that LJM partners had the ability to remove Fastow as the general partner or managing partner. This power was consistent with Causey's understanding of how Enron would approach the control issue as the general partner of JEDI. Causey did not recall what percentage of the partnership's capitalization had to be involved to trigger the limited partners' ability to remove Fastow. Causey recalled the concept of an advisory committee that would determine any LJM investments, but he did not remember when he learned this or whether it related to LJM1 or LJM2.

Causey discussed the concept of LJM1 with Fastow. He did not remember whether anyone else participated in these conversations. Causey did not recall whether Lay was involved in setting up LJM1. Skilling was involved in the concept of LJM1 and obtaining approval from the Board, but Causey did not remember any specifics about Skilling's role. Causey did not remember whether he knew that Andersen was pushing to give LJM's limited partners more power and authority after Enron started entering into transactions with LJM1. LJM2 was styled after LJM1. Causey did not recall any discussions about implementing procedures for LJM1 that had been adopted with respect to LJM2. Andersen provided front-end consultation and real-time auditing work at the time that LJM1 and LJM2 were established.

Causey did not recall discussing the potential conflict of interest in conducting transactions with LJM1 before the concept was presented to the Board. The Finance Committee considered the conflict of interest. Causey speculated that Skilling, legal, or someone else worked with Fastow on the conflict of interest issue before the concept was presented to the Board. Causey did not recall any discussion among Enron's personnel or at the Board level about whether it was a good or bad idea to have the Company's CFO involved in a private equity partnership that did business with the Company. There were discussions about whether the concept of LJM1 was acceptable, and Fastow addressed questions from Board members about that. The Board asked Causey whether Andersen had looked at LJM1 and whether it was acceptable from an accounting perspective. Causey told the Board that there were no particular accounting issues but there were disclosure requirements. Causey did not recall anyone on the Board or the Finance Committee expressing negative views about Fastow's role.

Fastow explained the idea of LJM1 to the Board. Causey did not recall specifically what Fastow said at the time, but Fastow explained LJM1 was going to be another source of capital. Causey did not get the sense that LJM1 was useful because it enabled Enron to transact deals that unrelated third-parties would not do. However, there was the idea that LJM1 would be more efficient than unrelated third-parties, although Causey was not sure whether his knowledge in this regard was based on his recollection at the time or things he learned in connection with preparing the November 2001 8-K.

Cash was responsible for performing whatever audit work was necessary. From an accounting viewpoint, LJM1 was acceptable, and LJM2 was viewed as routine. Fastow thought LJM2 was necessary because it would be another source of capital. The outside equity in LJM2 was much larger. Causey did not recall any issues regarding LJM2's governance or the partnership's structure.

Causey was aware that Kopper was buying out Fastow's interest. Fastow told Causey that he was going to sell his interest in LJM to Kopper. It sounded good to Causey. Enron was getting a few more questions than it wanted to have about the related-party nature of transactions with LJM2. Kopper's buyout would eliminate the related-party nature of the transactions. The resulting disclosure would be different and have an impact. Causey did not recall the reason given for Kopper buying out Fastow's interest, but the Company wanted the related-party issue to go away. Causey did not know if non-disclosure was the motivation behind this buyout. However, Causey liked the fact that he would no longer have to deal with these related-party disclosure issues. Causey was involved in the accounting for the buyout, but he was not involved in the decisions about whether it should occur or how it should take place.

Kopper's buyout was not related to Raptor's capitalization problems, and the Company's problems with Raptor did not drive the desire to have less disclosure – the Company wanted to put to rest concerns raised by McMahon and others about related-party transactions. To Causey's knowledge, there was no thought given to selling Fastow's interest to someone who was not associated with Enron; no one presented this as an alternative to Causey. Fastow could do whatever he wanted with his interest. Enron made no promises to Fastow or Kopper. The buyout was going to be a transfer of Fastow's interest to Kopper with no strings attached. There was no accounting for Enron to do with respect to the transfer. Kopper and Fastow made written representations regarding the transfer, and Causey believed that they represented that Fastow would not finance Kopper's acquisition. If Fastow had financed Kopper's purchase, Fastow's conduct would be inconsistent with Fastow's representations. Causey limited his review to Fastow's and Kopper's representations. Causey had received a signed draft of their representations, but Skilling left Enron before Causey could show it to Skilling. The draft document should still be around.

Causey did not communicate with analysts, but instead referred any analyst calls to Koenig.

LJM1 Transactions

Rhythms Net

RhythmsNet was LJM1's first transaction with Enron. The purpose was to hedge Enron's interest in Rhythms. Enron had in-the-money forwards of Enron stock. Some of these shares were delivered to LJM1 and, in return, Enron received compensation in the form of a derivative on Rhythms. This transaction gave birth to LJM1. After a put was in place for a short period of time, accounting rules for derivatives were utilized. The put was not perfect from a hedging perspective, and the put had to be improved through a series of other derivative transactions. LJM1's credit capacity to support the derivative transactions was based on restricted Enron shares that were contributed to LJM1 and LJM1's equity.

Causey did not recall whether Enron wrote some puts to LJM. LJM wrote some puts to Enron, but some might have gone the other way. Enron attempted to hedge its overall exposure to Rhythms with derivatives on Rhythms, not Enron stock. Causey did not recall who, besides Fastow, had contemplated these derivative transactions and speculated that Glisan may have contemplated them.

Fastow discussed the concept of LJM1 and the Rhythms transaction with Causey. During this conversation, Fastow raised the concept of using Enron stock to hedge Enron's positions. Skilling was concerned about the volatility of Rhythms and was also interested in hedging Rhythms. Enron viewed itself as a risk management company, and Skilling viewed Rhythms as a risk that he did not want. Skilling had more of an oversight role and a greater participation in the transaction with Fastow than Causey. Causey did not know whether Lay had any role in the Rhythms transaction.

Glisan, Mike Deville, and Bob Butts worked with Causey's valuation people on pricing the puts. PricewaterhouseCoopers ("PwC") also did some work on valuation, but Causey was not sure whether PwC's work was related to the initial transaction or all the puts. Causey did not work with Vince Kaminski's valuation group directly. Causey did not hear anything about making the put transaction as expensive to Enron as possible, nor could he imagine a reason why any Enron person would want to make the put as expensive to Enron as possible.

Causey did not know whether Enron's Rhythms transaction with LJM1 would have been available commercially. He recalled that the issue for Enron was whether it could do anything to hedge Rhythms. Causey recognized a unique aspect was that LJM1 was not going to cover the position. Causey agreed that conceptually it would have been difficult to hedge Rhythms commercially. He did not think that anyone pursued the possibility and would not expect anyone to have pursued it, but he did not know for sure. Causey could not say that there were no third-parties that would enter into the Rhythms transaction with Enron, but he understood that there was a restriction (*i.e.* a lock-up period) precluding Enron from hedging Rhythm shares with investment banks. Someone in the legal department had concluded that the transaction with LJM1 would not be a problem.

Glisan and perhaps Kevin Garland were involved in the Rhythms transaction. Others were involved, but Causey was not certain who they were. Causey did not recall any discussions about how the puts would become useless if both Enron and Rhythms stock declined in value, but the risk was obvious. Causey assumed that Enron's valuation people and PwC evaluated this risk.

Causey recalled generally in early 2000 that, because of the volatility, the structure's credit capacity was tight. Glisan, Deville, and Butts were involved in unwinding the transaction. Causey did not recall whether there were discussions about the potential credit risk and that a credit reserve might be needed, but he remembered considering the possibility. He did not recall anyone quantifying by percentage the chance of failure specifically, but different scenarios were analyzed. There were discussions about which valuation analysis would be used – the probabilistic or deterministic analysis – and Enron and Andersen debated about which analysis to use. Causey attended a meeting with Andersen in Chicago where John Stewart, Rick Petersen, and the Andersen team argued in favor of using a deterministic analysis while he argued in favor of the probabilistic method. The purpose of the meeting was not to discuss this transaction specifically, but to enter into an ongoing dialogue with Andersen so that they would understand Enron's business better and they could discuss emerging issues. At the end of the day, Enron went with Andersen's approach. Causey speculated that Duncan, Butts, Wes Colwell, Faldyn, and/or Ryan Siurek attended. Causey did not recall whether Enron had booked reserves. He recalled Deville working on the mechanics to have the Rhythms stock registered and then sold. Enron felt it could be paid for its hedge and that there was no reason not to unwind the Rhythms hedge.

Causey was charged with the responsibility of making sure that the unwind happened. He did not recall who had charged him with this responsibility. Deville and Butts assisted Causey. Causey and Fastow discussed how to make the unwind happen. Fastow made it clear to Causey and the Board that Fastow had no interest in the Enron stock, which Causey had interpreted to mean that Fastow had no residual interest in the Rhythms unwind. Fastow negotiated with his partners in LJM, provided the numbers to Causey, and Causey compared and eventually accepted them. Causey and Fastow discussed the terms that Fastow's limited partners would agree to. Their communications were verbal, and there are no written records memorializing them. Causey did not remember whether Skilling played any role in the Rhythms unwind, and he did not believe that Lay had any role. Lay would have known about Rhythms, the hedge, and the initial transaction with LJM1 from Board meetings, but Causey did not know whether Lay knew about the unwind. Sutton was Vice Chairman at the time and took a fairly active role in managing the Company, and Causey went to Sutton for approvals. To Causey's knowledge, neither the Board nor any Board committee was told about the unwind. Rhythms had already been hedged, and it would have been routine to close out the transaction.

Causey described the unwind based, in part, on his refreshed recollection during the past two months. The derivative transactions were cancelled and Enron received shares and cash. Causey did not know why Enron gave LJM a put on ENE at $71 for no consideration when ENE was trading at $67. Causey only recalled that Fastow worked with two partners on the buyout. Causey understood that CSFB had agreed to the buyout before NatWest. The values of Enron and Rhythms stock were moving, and Enron gave the put to LJM to freeze things so that negotiations could continue and the unwind would occur.

Causey did not know whether Enron had paid full unrestricted value for Enron shares even though there had been a discount on the shares when they were given to LJM at the beginning. He was focused on settling the derivatives on Rhythms, which did not involve Enron stock. He did not think the restriction on Enron shares was a pertinent fact relative to the settlement of four to five derivatives. Causey would have to speculate why Enron paid full value for restricted Enron shares. However, he, Butts, and Deville attempted to settle the transaction on terms favorable to Enron. Causey speculated that Enron lifted the restrictions on Enron stock during the unwind, because the restrictions may not have been important to Enron. They might have been more focused on the value that Enron was receiving. Butts, Deville, and Glisan would know more about why the restrictions might have been lifted. Causey did not remember whether Enron's valuation people were involved in the unwind.

CSFB was bought out first for $10 million, and NatWest was bought out second for $20 million. NatWest was going through some kind of change. Enron lent $10 million in connection with the first buyout but played no role in the second buyout. Causey assumed that LJM bought out the first partner's interest. Causey did not hear anything at that time about Enron people investing in the partnership interests. Causey signed a lot of documents relating to the unwind, but he did not remember whether those concerned the buyouts.

Cuiaba

In or around September 1999 when Enron sold an interest in Cuiaba to LJM1, Causey was not overly involved in the transaction. Cuiaba, a power plant in Brazil, was under construction at that time. Enron had a South American business unit, which wanted to sell an interest in Cuiaba. Causey did not know how LJM1 came to be the counterparty. Enron's business units considered LJM1 a potential party with whom to transact business; how these business units approached LJM1 was their decision. LJM1 was not set up for the Rhythms deal alone, but rather Enron contemplated doing other deals with LJM1.

Enron's South American business unit was selling gas with the Cuiaba entity. There was value in the contract, but some of that value had not been recognized because Enron owned greater than fifty percent of Cuiaba. The South American business unit wanted to reduce Enron's ownership interest in Cuiaba and, as a result, some of the resulting non-affiliated value could be recognized. Causey was aware of this impact and a general interest in minimizing Enron's interest in these types of plants and international assets. Causey did not recall the magnitude of the sale's impact on Enron's finances. He remembered that the sale of Enron's interest in Cuiaba did not result in much gain or loss and speculated that it probably had a minimal impact.

Causey did not remember whether he included the sale of the Cuiaba interest to LJM1 in his presentation to the Board committee regarding LJM transactions. He was aware of this transaction from an accounting perspective, and he addressed at that time the issue of the impact of the deal on Enron's gas contract. He was responsible for informing the Board whether the accounting for the LJM transactions was appropriate. In carrying out this responsibility, he spoke to the accounting people involved and monitored whether there were willing participants on both sides of the transaction. There was no reason for the business unit not to negotiate well on behalf of Enron with LJM. He did not know whether he spoke to those negotiating on behalf of Enron about the substance of the transaction. He spoke once or twice with Kent Castleman, who was stationed in Sao Paulo at the time, but Causey did not recall any specifics about their conversations. Causey did not remember whether Cheryl Lipshutz was involved in the Cuiaba transaction, and it would surprise him if she was. He was not sure which side she would have been negotiating for. It was common for people who reported indirectly to Fastow, to negotiate with LJM on behalf of Enron. Under Enron's matrix organization, it was not unusual for finance people in various business units to be involved in these transactions.

Causey did not remember any assurance by Enron at the time of the sale that LJM1 would not lose any money. There was some noise later coming from Fastow at some point that, if Enron did not market LJM1's interest within a certain period, LJM1 would be taken out of the transaction or receive a rate of return. Causey told Fastow that he did not understand why LJM1 would be allowed a higher rate of return. He recalled Fastow pushed this point in 2000. Causey did not challenge Fastow's understanding. Causey interpreted Fastow's statement as Fastow's expectation that LJM1 was not going to be stuck with a plant and not as an Enron guarantee to LJM1. Causey did not recall whether Fastow had identified the Enron person with whom he had this understanding. The transaction was not successful, Cuiaba was not remarketed, and LJM1 was bought out. Causey assumed that LJM1's rate of return was determined by the sale agreement, and he assumed that LJM1 was not taken out at a higher rate of return. If Fastow had received assurances that LJM1 would not lose money, Causey speculated that it would have had a very minimal impact on Enron's gain or losses, but he would have to think through its impact on Enron's accounting of the transaction.

Causey did not recall any other buyouts contemplated or suggested by Fastow. He did not remember any guarantee involved with the CLO transaction, Nowa Sarzyna, Bob West, or MEGS.

LJM2

Raptors I, II, and IV

Enron could hedge $1 billion with an entity that only had $30 million of capital, because LJM2 had rights to more than $30 million. LJM2 had $41 million in proceeds from a put that it wrote to Enron and rights to shares that could have increased in value.

There was significant work done on the Raptor structure to determine that it was acceptable from an accounting standpoint. Work was done to obtain reasonable valuations. Both Skilling and the Board wanted to do the transactions. Causey was not generating the ideas; he was doing the accounting for them. There was a question of whether the structure had the wherewithal to perform. In addition to Skilling, Glisan, and Fastow, both Siurek and Faldyn would be familiar with the accounting issues; Siurek facilitated getting the valuations.

From an accounting perspective, the hard issues were compliance with the SPE rules, applying the SPE rules once LJM received its initial return, the initial put on Enron stock, and the contribution or sale of equity from Whitewing, if available, to Raptor and receipt in value from Enron. With respect to the SPE rules, the issue was basically the 3% test. Once capital was put in, the question was whether it was a substantial enough investment to meet the 3% test. The equity test was based on the value of the assets placed in the venture plus the notional value of the total derivatives. The $30 million plus derivatives on merchant investments entered into over time amounted to more than 3% at some point. The 3% was calculated in a conservative manner, because the notional value of the derivatives was considered. Causey did not remember thinking that they needed more than 3% equity to set up a workable structure.

Causey could not think of an independent, commercial reason for Enron to purchase a put on its own stock, as it did in the Raptor I, II and IV transactions. The purchase should be considered part of the whole transaction, and Causey did not evaluate this purchase. Causey's view at the time was that the put was in place, and there was risk given that the price of the stock could decrease. In the context of the whole deal, Skilling was willing to do it. Causey did not know if Skilling had a business purpose in mind for buying a put on Enron's stock. There was no discussion of accounting for the $41 million paid to LJM. There was more of a discussion about the real risk that was transferred and an earnings event involving a return "on" capital to LJM2, as opposed to "of" capital. From Enron's perspective, it was a return "on" capital. Causey did not hear at the time that LJM2 was telling its investors that it was a return "of" capital.

Causey did not recall any discussion of the consequences of purchasing a put on some 7 million shares of Enron stock from an entity that had only $30 million equity plus $41 million from a payout by Enron, and whether such an entity would have the capacity to pay if the stock dropped more than $10 per share. He recalled PwC's valuation opinion on Raptor I, but he did not remember any specific details. Siurek worked with Enron's valuation people, including Stinson Gibner, on the valuation of the put.

There was some concept of paying LJM2 a fee to cover certain expenses, but Causey did not recall any specific discussion or negotiation about the $250,000 annual fee to LJM2 for Raptor. Enron did not cover LJM2's actual expenses but paid LJM2 the fee directly. Causey did not recall whether Enron paid any of LJM2's expenses directly. He also did not remember any discussion of what impact Enron's payment of an annual fee would have on the 3% rule or any consideration of whether Enron should be reimbursing LJM2 for expenses as opposed to making direct payments to providers of services.

Enron did not think about whether Raptor would last when the discount on the shares of stock would be consumed over its life by the interest accruing on the notes. From Enron's perspective, Enron evaluated Raptor's capacity to pay based on the restriction discount, the note receivable, and the potential exposure on derivative transactions. This evaluation was known as the Raptor Position Report. It was not inevitable that Raptor's capacity would be consumed over time as the interest on the notes accrued and Raptor's liabilities increased. There were exposures from derivative transactions that could go in a different direction. Causey tried to keep an eye on whether any problems arose.

LJM2 had the right to put back its interest in Enron stock at fair market value. If the stock were to drop or LJM2 did not get its return, Enron would pay LJM2 the fair value for its equity interest, which could still result in a loss to them. Causey was not aware of any calculation done on the risk of loss to LJM2. There was a calculation done on the value of the put. Siurek worked with Gibner on the valuation. Causey did not know what Siurek and Gibner did, but Siurek understood the limits of the transaction better than anyone.

Enron's investment in Raptor was based on the cost, not equity, method. Causey did not remember details about the consideration of which methodology to use. He raised the issue and it was an important question; the equity method would have created volatility. Causey worked with Andersen on it. Carl Bass communicated to Andersen that the cost method was appropriate. As far as Causey knows, Andersen was aware of everything regarding the Raptor transactions. The basis for asserting the cost method was that Enron had rights to appreciated equity beyond the amount allocated to LJM2. Enron's lack of significant influence was a factor in determining that the equity method was not appropriate. If Enron had received distributions from derivative transactions and accounted for them under the cost method, they were advised that the distributions would be recognized as earnings. Causey observed a contrast between Andersen's position in the Raptor transactions and its position in JEDI, but he did not raise it with Andersen at the time.

Causey did not remember any Enron employee who disagreed with the Raptor transactions at the time.

The investments that Enron hedged in Raptor were volatile. Causey was not involved in the selection of these investments. Different business units wanted to hedge different investments to a point where the desire to hedge outstripped the capacity. Different people approached Causey requesting capacity, and Causey was planning to have Skilling select which investments to hedge. However, Causey never had to go to Skilling because they did not run out of capacity.

Causey had not heard that any investments in Raptor were backdated. Sometimes trades were made and then documented one week or one month later. Causey did not remember whether all transactions relating to Raptor I were documented on August 3. One or two technical investments were made and then a number of North American investments were made soon thereafter.

Causey did not remember that Raptor was thought of as a means by which Enron would be able to avoid disclosing investments that lost a lot of money so long as the market price of Enron's stock remained high. It was not the way that Causey viewed Raptor. It was not some big plan to enter into bad investments. Looking at it today, Causey could understand how others view Raptor as a means by which companies avoid disclosing losses to the investment community. However, Raptor was not designed to avoid disclosing losses.

Raptor III

The New Power Company ("TNPC") shares were valued at $10.75 before the IPO. The shares were transferred into a SPE at $10.75, and a few days later there was an initial public offering that raised the shares to a higher value, and that increased the value in the SPE. Between the time that the shares entered the SPE and the IPO, it was unclear what the price of the shares would be. Causey did not remember how the value of TNPC's shares was calculated before the IPO or whether Enron had obtained a valuation opinion.

Raptor's credit capacity was based on its long position in TNPC stock. Enron hedged by having Raptor write hedges to Enron. If TNPC's value went down, Raptor III also lost value. No valuation was necessary for this transaction. Whether this transaction was an effective hedging technique is another question, but it was one that Skilling was aware of and decided to go forward with. Fastow, Skilling, Siurek, Causey, and possibly Glisan and Jimmie Williams were involved with Raptor III.

Raptor Restructure and Unwind

Raptor III started to run into a series of credit problems because TNPC's value dropped. In August 2000, there was a costless collar placed on Enron's stock to minimize volatility. Enron would underwrite the derivative if it fell out of the zone of the collar. It was a costless collar with no premium. Siurek and the valuation group facilitated the work on valuing the costless collar. Causey did not know how the costless collar could have an $81 floor when Enron's stock was trading at $81 at the time. Causey did not recall any consideration of the economics of letting LJM benefit from a discount and having a costless collar. He did not know and did not remember whether there was a waiver of the restriction on hedging.

The Raptor restructuring took place in the first quarter. Siurek developed the restructuring to solve a credit capacity problem. Enron recognized that it might have a credit capacity issue and have to recognize an impairment if a solution was not developed. Causey did not remember the amount at stake, and he did not recall whether the impairment occurred before a solution was put in place. Cross-collateralization within the vehicles, otherwise known as "topping off," was implemented to deal with the problem. Whitewing shares were unavailable to give to Raptor. As a result, Enron transferred in 12 million shares that had come in from the consolidation of JEDI and, in return, Enron received a note receivable. Causey did not recall whether these were restricted shares. Causey did not remember consideration of the basis for discounting the value of the shares when a collar was placed on the shares simultaneously. Looking at it today, Causey believed that the restriction on the sales was appropriate because it precluded the shares from being sold on the market. However, he recognized that the amount Enron charged for the shares could have been higher.

If a structure was created that could not lose money, there would be no equity at risk. Although discounted shares were put in place that were also collared, there were other things at risk such as derivative transactions. It was not a riskless transaction.

With regard to Raptor IV not having any derivative transactions at the time of the restructuring, Causey was not part of any discussions about the risk that was involved. He was aware of the requirements regarding the final $35 million payment, but he was not involved in determining that price.

Causey believed that cross-collateralization among the Raptors did not transfer LJM2's equity at risk from one Raptor vehicle to another. LJM2 had value in two of the entities of roughly $30 million each, and the negotiated windup payment in the aggregate was $35 million. Siurek and other finance people were involved in these transactions. Because Fastow no longer had an interest in LJM, Fastow was the lead negotiator on behalf of Enron and Causey kept apprised of the negotiations, which were acceptable from his perspective.

Miscellaneous

Davidow showed Causey a two-page e-mail from Vince Kaminski to Andersen dated October 2, 2001. Causey responded that he had heard that Kaminski had an issue with Raptor. Causey did not talk to Kaminski about it. The Raptors were going away, and there did not seem to be any point speaking with Kaminski. Causey had a vague recollection that Duncan referred to Kaminski's e-mail during one of their conversations and said that they must make sure they were comfortable with the valuation. Through subsequent valuation exercises, Causey heard about Kaminski's e-mail from Siurek, but by that time the issue was moot. Causey was not aware of any effort to prevent Kaminski from speaking directly with Andersen after sending that e-mail. Kaminski raised the issue during a recent meeting of managing directors, and Causey indicated to Kaminski that they might work together on this, but that never happened.